BEFORE THE ARIZONA CORPORATION COMMISSION

MARC SPITZER
Chairman
JIM IRVIN
Commissioner
WILLIAM A. MUNDELL
Commissioner
JEFF HATCH-MILLER
Commissioner
MIKE GLEASON
Commissioner

IN THE MATTER OF QWEST CORPORATION'S COMPLIANCE WITH SECTION 252(e) OF THE TELECOMMUNICATIONS ACT OF 1996.	Docket No. RT-00000F-02-0271

POST-HEARING BRIEF OF THE RESIDENTIAL UTILITY CONSUMER OFFICE

The Residential Utility Consumer Office ("RUCO") respectfully submits its post-hearing brief.

RESPECTFULLY SUBMITTED this 1st day of May, 2003.

Daniel W. Pozefsky
Staff Attorney

AN ORIGINAL AND **THIRTEEN** COPIES
of the foregoing filed this 1st day
of May, 2003 with:

Docket Control
Arizona Corporation Commission
1200 West Washington
Phoenix, Arizona 85007

COPIES of the foregoing hand delivered/
mailed this 1st day of May, 2003 to:

Jane L. Rodda
Administrative Law Judge
Hearing Division
Arizona Corporation Commission
400 West Congress Street, Room 222
Tucson, Arizona 85701

Maureen Scott
Legal Division
Arizona Corporation Commission
1200 West Washington
Phoenix, Arizona 85007

Ernest Johnson, Director
Utilities Division
Arizona Corporation Commission
1200 West Washington
Phoenix, Arizona 85007

Timothy Berg
Theresa Dwyer
Fennemore Craig, P.C.
3003 North Central Ave., Suite 2600
Phoenix, Arizona 85012

Maureen Arnold
Qwest Corporation
3033 North Third Street, Room 1010
Phoenix, Arizona 85012

Andrew Cain
Qwest Corporation
1801 California Street, 4900
Denver, Colorado 80202

Michael M. Grant
Todd C. Wiley
Gallagher & Kennedy, P.A.
2575 East Camelback Road
Phoenix, Arizona 85016-9225

Mark Dioguardi
Tiffany and Bosco, P.A.
500 Dial Tower
1850 North Central Avenue
Phoenix, Arizona 85004

Curt Huttsell
Electric Lightwave, Inc.
4 Triad Center, Suite 200
Salt Lake City, UT 84180

Jeffrey W. Crockett
Snell & Wilmer
One Arizona Center
Phoenix, Arizona 85004-0001

Darren S. Weingard
Stephen H. Kukta
Sprint Communications Company L.P.
1850 Gateway Drive, 7th Floor
San Mateo, California 94404-2467

Andrew O. Isar
TRI
4312 92nd Ave., N.W.
Gig Harbor, Washington 98335

Cox Communications
Cox Arizona Telecom LLC
20401 North 29th Ave.
Phoenix, Arizona 85027

Richard M. Rindler
Morton J. Posner
Swidler, Berlin, Shereff, Friedman, LLP
3000 K Street, NW, Suite 300
Washington, DC 20007-5116

Raymond S. Heyman
Roshka Heyman & DeWulf, PLC
One Arizona Center
400 East Van Buren Street, Suite 800
Phoenix, Arizona 85004

Charles Kallenbach
American Communications
Services, Inc.
131 National Business Parkway
Annapolis Junction, Maryland 20701

Thomas F. Dixon
Worldcom, Inc.
707 17th Street, Suite 3900
Denver, Colorado 80202

Richard S. Wolters
AT&T &TCG
1875 Lawrence Street, Suite 1500
Denver, Colorado 80202

Joyce Hundley
U.S. Department of Justice
Antitrust Division
1401 H St., NW, Suite 8000
Washington, DC 20530

Joan Burke
Osborn Maledon
2929 North Central Ave., 21st Fl.
P.O. Box 36379
Phoenix, Arizona 85067-6379

Daniel Waggoner
Davis Wright Tremaine
2600 Century Square
1501 Fourth Ave.
Seattle, Washington 98101-1688

Douglas Hsiao
Jim Scheltema
Blumenfeld & Cohen
1625 Massachusetts Ave., N.W.
Suite 300
Washington, DC 20036

Diane Bacon, Legislative Director
Communications Workers of America
5818 North 7th Street, Suite 206
Phoenix, Arizona 85014-5811

Mark N. Rogers
Excell Agent Services, L.L.C.
PO Box 52092
Phoenix, Arizona 85072-2092

Traci Grundon
Davis Wright Tremaine, LLP
1300 S.W. Fifth Ave., Suite 2300
Portland, Oregon 97201

Kimberly M. Kirby
Davis Dixon Kirby LLP
19200 Von Karman Avenue
Suite 600
Irvine, California 92612

M. Andrew Andrade
5261 S. Quebec Street, Suite 150
Greenwood Village, Colorado 80111

Al Sterman
Arizona Consumers Council
2849 East 8th Street
Tucson, Arizona 85716

Brian Thomas
Time Warner Telecom, Inc.
223 Taylor Avenue North
Seattle, WA 98109

Jon Poston
Arizonans for Competition in Telephone
Service
6733 East Dale Lane
Cave Creek, Arizona 85331-6561

Eric S. Heath
Sprint Communications Company L.P.
100 Spear Street, Suite 930
San Francisco, CA 94105

Philip Doherty
545 S. Prospect St., Suite 22
Burlington, VA 05401

Andrea Harris
Allegiance Telecom Inc. of Arizona
2101 Webster, Suite 1580
Oakland, CA 94612

Kevin Chapman
SBC Telecom
300 Convent St., Room 13-Q-40
San Antonio, TX 78205

Richard Sampson
Z-Tel Communications
601 S. Harbour Island, Suite 220
Tampa, FL 33602

Gary L. Lane
6902 E. First St., Suite 201
Scottsdale, AZ 85251

Steven Strickland
SBC Advanced Solutions, Inc.
1010 North St. Mary's, Room 13-I
San Antonio, TX 78215

Richard Kolb
One Point Communications
150 Field Dr., Suite 300
Lake Forest, IL 60045

Steven Duffy
Ridge & Isaacson
3101 N. Central Ave., Suite 1090
Phoenix, AZ 85012

Dennis Ahlers
Eschelon Telecom
730 Second Ave South, Suite 1200
Minneapolis, MN 55402

Dennis Doyle
Arch Communications Group
1800 West Park Dr., Suite 250
Westborough, MA 01581-3912

David Conn
McLeod USA
P.O. Box 3177
Cedar Rapids, IA 52406-3177

Frederick Joyce
Alston & Bird, LLP
601 Pennsylvania Ave., NW
Washington, DC 20004-2601

John Munger
Munger Chadwick
333 North Wilmot, Suite 300
Tucson, AZ 85711

Deborah Harwood
Integra Telecom of Arizona
19545 NW Von Newman Dr., Suite 200
Beaverton, OR 97006

Bob McCoy
William Local Network
4100 One Williams Center
Tulsa, OK 74172

Teresa Tan
Worldcom, Inc.
201 Spear St., 9th Floor
San Francisco, CA 94105

Rodney Joyce
Shook Hardy & Bacon, LLP
600 14th St., NW, Suite 800
Washington, DC 20005-2004

Diane Peters
Global Crossing
180 South Clinton Ave
Rochester, NY 14646

Gerry Morrison
Map Mobile Communications
840 Greenbrier Circle
Chesapeake, VA 23320

Metrocall, Inc.
6677 Richmond Highway
Alexandria, VA 22306

Paul Masters
Ernest Communications
6475 Jimmy Carter Blvd, Suite 300
Norcross, GA 30071

Rex Knowles
XO
111 E. Broadway, Suite 100
Salt Lake City, UT 84111

Teresa Ono
AT&T
795 Folsom St., Room 2159
San Francisco, CA 94107-1243

Penny Bewick
New Edge Networks
P.O. Box 5159
Vancouver, WA 98668

David Kaufman
E.Spire Communications
343 W. Manhattan St.
Santa Fe, NM 87501

Bob Edgerly
Nextel West Corporation
2001 Edmund Halley Dr.
Reston, VA 20131

McLeodUSA Telecommunications Services
Attention: Law Group
P.O. Box 3177
Cedar Rapids, IA 52406-3177

Steven Sager
McLeodUSA Telecommunications Services
215 S. State St.
Salt Lake City, UT 84111

Gary Kopta
Davis Wright Tremaine LLP
1501 Fourth Avenue
Seattle, WA 98101

Thomas H. Campbell
Lewis & Roca
40 North Central Avenue
Suite 1900
Phoenix, AZ 85004

Harry Pliskin
Senior Counsel
Covad Communications Company
7901 Lowry Blvd.
Denver, CO 80230

Jacqueline Manogian
Mountain Telecommunications, Inc.
1430 W. Broadway Road, Suite A200
Tempe, AZ 85282

By _____
Jennifer Rumph

TABLE OF CONTENTS

I. INTRODUCTION

Non-discrimination by incumbent local exchange carriers ("ILECs") is a bedrock principle of the Telecommunications Act of 1996 (the "Act"). The interconnection agreement filing and pick-and-choose requirements of 47 U.S.C. § 252 were passed by Congress to implement it's intent to guarantee adherence to these bedrock principles. The facts and evidence in this case, however, show that Qwest Corporation ("Qwest")[1] made a practice of entering into confidential interconnection agreements with Competitive Local Exchange Carriers ("CLECs") that it intentionally did not file with the Arizona Corporation Commission (the "Commission") as required by 47 U.S.C. § 252(a) and (e). Qwest formed business relationships which included preferential and discriminatory terms with two of its largest wholesale competitors, McLeodUSA Telecommunications Services, Inc. ("McLeod") and Eschelon Telecom, Inc. ("Eschelon"). In the process, Qwest not only violated the Act, but Qwest, Eschelon and McLeod violated state law and the Commission's rules.

Qwest, Eschelon and McLeod ("the parties") gained substantial benefits by entering into these agreements. Qwest increased its own revenues, kept McLeod and Eschelon on its network, and prevented McLeod and Eschelon from participating in public consideration of whether Qwest should be able to re-enter the interlata long distance market through the process set for in 47 U.S.C. § 271 ("§ 271"). Eschelon and McLeod enjoyed, among other things, lower interconnection rates than their competitors received.

[1] Unless otherwise noted, "Qwest" refers collectively to Qwest Corporation, its affiliates and subsidiaries, and U S WEST Communications, Inc., the predecessor in interest to Qwest.

The parties' conduct has impeded the development of real competition in Arizona. By offering favorable and discriminatory terms only to those CLECs that would, in turn, promote Qwest's regulatory agenda, Qwest has sent a clear message to this Commission that it will not comply with the law nor respect this Commission's authority and responsibilities to implement the law. Moreover, the lack of McLeod and Eschelon's participation in Arizona's § 271 proceedings tainted the integrity of that process.

As willful participants, McLeod and Eschelon are no less responsible for the negative impact on the development of competition in Arizona. Without McLeod and Eschelon, Qwest would not have been able to carry out its objectives. The business arrangements between the parties substantially benefited each member at tremendous expense to the development of competition in Arizona. Unfortunately, the real loser is the Arizona consumer.

The overwhelming evidence in this case can lead this Commission to only one conclusion: Qwest knowingly and intentionally violated 47 U.S.C. § 251 and § 252, and Qwest, McLeod and Eschelon violated A.R.S § 40-203, A.R.S. § 13-2310, A.R.S. § 2311, and A.A.C. R-14-2-1112.

While there is no adequate remedy for the harm Qwest has done to the Arizona regulatory process, the cause of competition in Arizona and the public trust, the Commission has broad regulatory powers to implement appropriate remedies. The Commission should impose remedies which would not only deter Qwest and CLECs from engaging in similar conduct in the future, but will also remediate the

negative impact that the parties' conduct has had on competition as well as the integrity the Commission's § 271 process.

II. THE UNFILED AGREEMENTS

In all, Staff has identified 96 unfiled agreements in this proceeding. Joint Exhibit 1.[2] RUCO has focused its investigation on the following unfiled agreements ("core agreements") that Qwest executed with McLeod and Eschelon[3]:

1. In or about October 2000, Qwest and McLeod entered into an oral agreement (McLeod Agreement I). The parties agreed that Qwest would provide McLeod with a discount/refund of up to 10% on all purchases made by McLeod from Qwest. (R-1C, MDC-2C at pages 6-10). Another component of the oral agreement was McLeod's agreement to remain neutral regarding Qwest's § 271 application. Id., at page 10.

---

[2] For ease of reference, trial exhibits will be identified similar to their identification in the Transcript of Proceedings. The Transcript volume number, page number, line number will identify references to the Transcript. For example, line 10 on page 200 of the transcript will be cited as: Transcript, Volume 1 at 200:10. For hearing exhibits which include a deposition, reference will be to the exhibit number, page number, and line number. For example, line 10 of page 200 of the deposition of Richard Smith attached as CD-62 to Mr. Deanhardt's direct testimony would be cited as: R-1B, CD-62 at 200:10. Where the deposition includes an exhibit the exhibit will be referenced as deposition exhibit #. For example, the fifth exhibit (RUCO 5) to Mr. Smith's deposition in CD-62 of Mr. Deanhardt's direct testimony will read as: R-1B, CD-62, deposition exhibit RUCO 5. For hearing exhibits which include an affidavit, reference will be to the exhibit number, and paragraph number. For example, reference to the second paragraph of Mr. Blake Fisher's affidavit attached as Exhibit MDC-2C to the direct testimony of Marylee Diaz Cortez will be cited as: R-1C, MDC-2C, paragraph 2.

[3] RUCO acknowledges that there were a significant number of unfiled agreements that Qwest executed with other CLECs. Those agreements, set forth in Joint Exhibit 1, were not addressed as part of RUCO's case in chief. RUCO's comments regarding Qwest's filing obligations concern only the McLeod and Eschelon agreements listed here. To the extent necessary, RUCO will refer to, identify and explain other unfiled Eschelon and McLeod agreements throughout this brief.

2. On October 26, 2000 Qwest and McLeod entered into a *Purchase Agreement* ("McLeod Agreement II", R-1C, MDC-2A). In Section 2 of that agreement, McLeod agreed to buy at least **[BEGIN TRADE SECRET]** **[END TRADE SECRET]** of telecommunications products from Qwest from October 2, 2000 to December 31, 2003. Id. ¶¶ 2.1, 2.2, 2.3.

3. On October 26, 2000, Qwest and McLeod entered into another *Purchase Agreement* ("McLeod Agreement III", R-1C, MDC-2A). In this agreement, Qwest agreed to pay McLeod **[BEGIN TRADE SECRET]**

[END TRADE SECRET] Id., ¶¶ 3.1, 3.2, 3.3. As will be more fully discussed in Section (VI)(B) of this brief, Qwest attempted to conceal the favorable pricing it was providing McLeod through this unfiled purchase agreement.

4. On October 26, 2000, Qwest and McLeod entered into an *Escalation Procedures and Business Solutions Letter* "McLeod Agreement IV", RUCO 8, Joint Exhibit 1, # 19. Section 2 of the agreement requires Qwest to send an executive at the vice-president level or above to attend quarterly meetings with McLeod to address, discuss and attempt to resolve unresolved business issues and disputes, anticipated business issues, and issues related to the parties' interconnection agreements and other agreements Id., Section 2.

Qwest agreed in Section 3 of the agreement to a six-level set of escalation procedures that gave McLeod access to Qwest's senior management, beginning with Qwest's vice-presidents and including Qwest's CEO, for resolving interconnection issues Id., Section 3. As part of those escalation procedures, Qwest also waived tariff limitations on damages and other limitations on actual damages in disputes with McLeod. Id.

5. On November 15, 2000, Qwest and Eschelon entered into an *Escalation Procedures and Business Solutions Letter.* ("Eschelon Agreement I" (R-1B, CD-62 - RUCO 9,[4] Joint Exhibit 1, #3). Section 1 of the agreement provides that the parties would agree to meet to develop an implementation plan. Eschelon agreed to not oppose Qwest's efforts to obtain § 271 approval or file any complaints with any regulatory body concerning issues arising out of the parties interconnection agreements, while the Plan was being developed and afterwards, provided the Plan was in place by April 30, 2001. Id., Section 1. Section 2 of the agreement requires Qwest to send a vice-president level or above executive to attend quarterly meetings with Eschelon to address, discuss and attempt to resolve unresolved business issues and disputes, anticipated business issues, and issues related to the parties' interconnection agreements and other agreements. Id., Section 2. Qwest agreed in Section 3 of the

[4] R-1B, CD # refers to the exhibit number attached to the direct testimony of Clay Deanhardt. Likewise, R-1C, MDC # refers to the exhibit number attached to the direct testimony of Marylee Diaz Cortez.

agreement to a six-level set of escalation procedures that gave Eschelon access to Qwest's senior management, beginning with Qwest's vice-presidents and including Qwest's CEO, for resolving interconnection issues. Id., Section 3. As part of those escalation procedures, Qwest also waived tariff limitations on damages and other limitations on actual damages in disputes with Eschelon. Id.

6. On November 15, 2000, Qwest and Eschelon entered into *Confidential Amendment To Confidential/Trade Secret Stipulation* ("Eschelon Agreement II, R-1C, MDC-5B, Joint Exhibit 1, #4). In this document, Qwest agreed:

   a. Provide Eschelon with a 10% discount/refund on all purchases made by Eschelon from Qwest, including the purchase of UNEs, tariffed services, switched access, unregulated services and all telecommunication services regulated by the Act. Id., Section 3. As discussed more thoroughly in Section VI (C) of this brief, Qwest attempted to conceal the discount/refund agreement in a sham "consulting" arrangement.

   b. Credit Eschelon $13.00 (or pro rata portion thereof) per UNE-platform line per month access for each month during which Qwest failed to provide Eschelon with accurate daily usage information. Id., ¶ 2.

Each of these agreements on its face created a concrete and specific legal obligation for Qwest to do something or refrain from doing something related to both

Qwest's obligations under 47 U.S.C. § 251(b) and (c) and its obligations under 47 U.S.C. §§ 271(c)(2). Despite that, however, Qwest did not timely file with the Commission any of the agreements containing these provisions as required by 47 U.S.C. § 252(a)(1), 47 U.S.C. § 252(e), and A.A.C. R-14-2-1112.

III. BACKGROUND

During the year 2000, McLeod and Eschelon were two of Qwest's largest resellers of telecom services. For several reasons, both McLeod and Eschelon wanted to change their billing platforms with Qwest. Transcript, Volume III at 594:11-17. Eschelon and McLeod had been reselling Qwest's Centrex service to their own customers. Id., at 594:4-7. Both Eschelon and McLeod were unhappy with reselling the Centrex product because of the cost and the low margin they realized from sales. With McLeod, the margins McLeod realized from resale were to thin for McLeod to sustain growth. R-1C, MDC-2C at ¶ 7. McLeod and Eschelon wanted to move away from reselling the Centrex service and provide service over an unbundled network element platform ("UNE-P"). They believed that the UNE-P would result in higher margins. Transcript, Volume III at 594:4-10. The UNE-P would also allow McLeod and Eschelon to collect their own access fees. Under resale, Qwest collected the access fees. This, in turn, provided McLeod and Eschelon with a new revenue stream. Id., at 594:18-25.

Qwest also recognized the value in maintaining a good business relationship with McLeod and Eschelon. According to Audrey McKenney, Qwest's Senior Vice-President of Wholesale Markets at the time, Qwest had just merged with US West

and wanted to promote its "new philosophy" of cooperating and being supportive of its wholesale providers. R-1C, MDC-3B at p. 19:15-18.

Specifically, with McLeod, Qwest wanted to keep McLeod on its network even if it was not getting full price[5]. Transcript, Volume III at 595:10-17. Qwest was aware that if McLeod took all of its customers off Qwest's network and put them on McLeod's new network, Qwest would suffer a large negative impact. R-1B, CD-4 63:4 – 63:8. Finally, Qwest was interested in McLeod's assurance that it would remain neutral in the § 271 proceeding.

McLeod and Qwest entered into negotiations in the late summer/early fall of 2000 to create a new business relationship that would be beneficial to both. The new Qwest, according to its representatives, wanted to keep and even increase McLeod's traffic on its network. R-1B at 14, CD-3. Qwest wanted to "leverage" the wholesale markets and make McLeod the "flagship" wholesale carrier in Qwest's "footprint". R-1B, CD-3. McLeod, on the other hand, wanted to reduce costs and increase service quality. R-1B at 14, CD-3.

In the case of Eschelon, US West had been providing poor service to Eschelon prior to its merger with Qwest in 2000. R-1B, CD 62 at 9:8-13. Eschelon's relationship with US West and then Qwest continued to improve through the spring and summer of 2000. R-1B, CD-62 at 16:13-16. Like McLeod, one of Eschelon's main issues with Qwest was pricing. Specifically, Eschelon wanted to switch its customers to a new pricing platform (UNE-P or its equivalent). Eschelon's other

[5] McLeod was aware that it could convert its resold lines and move as much traffic off of Qwest's lines as possible thereby reducing its costs. R-1B at 14.

main issues were Qwest's level of service and escalation procedures. R-1B, CD-62 at 16:17 –17:23.

As with McLeod, Qwest wanted assurances from Eschelon that it would remain neutral in the § 271 proceedings. Eschelon was sensitive to Qwest's objective and considered as the trade-off how Qwest could help Eschelon financially. R-1B, CD-62, deposition exhibit RUCO 3 and deposition exhibit RUCO 4. The problem was that Qwest would not reduce the prices it charged Eschelon for UNE-Star below the level it considered publicly acceptable – that is, below the level it would let other CLEC's opt-into. R-1B, CD-62 at 42:18-21. So, instead, Qwest agreed to provide a "discount" to Eschelon for all of its purchases from Qwest, thereby achieving the price reduction sought by Eschelon. To conceal this discount, Qwest and Eschelon concocted the sham consulting agreement, which they intended to be a "unique" agreement, specific to Eschelon, and not available to other carriers. R-1B, CD-62 at 43:3-18. Richard Smith, Eschelon's President at the time states the parties' objective in his letter to Qwest dated November 5, 2000:

> I feel there is an opportunity to partner on process improvements. If we can develop this idea, put some teeth into it and incorporate it into our interconnection agreement and/or purchase agreement, we may also have a mechanism that makes it more difficult for any party to opt into our agreement.

R-1B, CD-62, deposition exhibit RUCO 4. Eschelon was not concerned about other carriers not having the same terms available to them, as required by the Act. R-1B, CD-62 at 43:24-44:2.

The parties documented their intent as well as their knowledge of the circumstances extensively. They clearly intended to create business relationships which were not available to other carriers. The underlying documentation is so detailed that there is no room for misinterpretation. As will be more fully discussed below, the parties enjoyed significant financial and other benefits.

IV. THE LEGAL ISSUES

The legal questions that must be answered by this Commission in this docket are:

1. Was Qwest's failure to file some or all of the terms and conditions contained in the core agreements (as well as the other unfiled agreements) a violation of 47 U.S.C. § 252(e) (the "Act") and A.A.C. R-14-2-1112 (the "Rule")?
   a. Did Qwest also violate A.R.S. § 40-203 by violating the Act and the Rule?
2. Did Qwest and McLeod and Qwest and Eschelon engage in a scheme to defraud this Commission in violation of A.R.S. § 13-2310 and A.R.S. § 13-2311?
   a. Did Qwest, Eschelon and McLeod also violate A.R.S. § 40-203 by violating A.R.S. § 13-2310 and A.R.S. § 13-2311?
3. What are the appropriate remedies?

A.R.S. § 40-203 provides as follows:

> **When the commission finds** that the rates, fares, tolls, rentals, charges or classifications, or any of them, demanded or collected by any public service corporation for any service, product or commodity, or in connection therewith, or **that the rules, regulations, practices or**

> **contracts, are unjust, discriminatory or preferential, illegal or insufficient, the commission shall determine and prescribe them by order**, as provided in this title. (Emphasis added)

The evidence presented in this case shows that Qwest, McLeod and Eschelon engaged in practices and entered into agreements which were illegal, discriminatory and preferential in violation of A.R.S. § 40-203. The agreements were illegal, discriminatory and preferential for the following reasons: (1) Qwest failed to file some or all of the terms and conditions contained in the unfiled agreements with the Commission for approval under 47 U.S.C. § 252(e), and A.A.C. R-14-2-1112; (2) by filing certain agreements and not filing others, Qwest, Eschelon and McLeod misrepresented to the Commission the true nature of their business relationships. The parties' misrepresentations were deliberate and intentional. The parties each benefited from their business relationships. The parties' unfiled agreements discriminated against other CLECs because the same terms and conditions were not made available to the other CLECs as required by the Act. The parties' conduct violated A.R.S. § 13-2310 and A.R.S. § 13-2311.

Among other things, RUCO is requesting that the Commission prescribe the parties' illegal practices and agreements. As set forth below, RUCO has proposed four remedies, all within this Commission's authority, to remediate the harmful effects that the parties' business relationships have had on competition and the integrity of this Commission's process.

Finally, the future of competition in Arizona would be further impeded by this Commission's failure to acknowledge and remediate the role that Eschelon and McLeod played in deceiving this Commission and undermining competition in

Arizona. This docket is about more than Qwest's filing obligations under the Act. Limiting the scope of the proceeding to that issue would be tacitly approve Eschelon and McLeod's conduct, and would send the message that it is all right for CLECs to enter into discriminatory agreements with the Incumbent Local Exchange carrier ("ILEC") since there will be no reprisal if discovered. The Commission must send the message that this type of conduct is egregious and that there will be consequences for anyone who participates.

V. 47 U.S.C. § 252 REQUIRES QWEST TO FILE ALL INTERCONNECTION AGREEMENTS WITH THE COMMISSION TO PREVENT DISCRIMINATION AGAINST NON-PARTY CLECs.

Qwest's obligations to file interconnection agreements are defined by: 47 U.S.C. § 252 ("Section 252" or "§ 252"), 47 U.S.C. § 251 ("Section 251" or "§ 251"), and A.A.C. R-14-2-1112. Section 252 requires Qwest to file all interconnection agreements with the Commission for approval under § 252(e).[6] Terms and conditions from approved interconnection agreements are then available for other CLECs to opt into under § 252(i).[7] Prior to the passage of the Act, the Commission adopted its own Rule requiring interconnection agreements to be filed with the

[6] Section 252(a)(1) permits ILECs to enter into negotiated agreements for interconnection, services or network elements and provides that "The agreement ... shall be submitted to the State commission under subsection (e) of this section." Section 252(e)(1) requires that "any interconnection agreement adopted by negotiation or arbitration shall be submitted for approval to the State commission."

[7] 47 U.S.C. § 252(i) requires "A local exchange carrier shall make available any interconnection, service or network element provided under an agreement approved under [§ 252] to which it is a party to any other requesting telecommunications carrier upon the same terms and conditions as those provided in the agreement."

Commission.[8]

As the FCC said in the *Local Competition Order*[9], one of the three primary goals of the Act is to open the local exchange and exchange access markets to competitive entry. The FCC explains that "competition in local exchange and exchange access markets is desirable, not only because of the social and economic benefits competition will bring to consumers of *local* services, but also because competition eventually will eliminate the ability of an incumbent local exchange carrier to use its control of bottleneck local facilities to impede free market competition."[10] (Emphasis in original). Congress sought to achieve this goal of preventing discrimination by ILEC's against CLECs through § 252(i) of the Act.[11] The FCC first addressed an ILEC's filing obligation with a state commission in its *Local Competition Order.* The FCC made it clear that there are no exceptions to § 252's filing requirements. All interconnection agreements must be filed. The FCC said:

> As a matter of policy, moreover, we believe that requiring filing of all interconnection agreements best promotes Congress's stated goals of opening up local markets to competition, and permitting interconnection on just, reasonable, and nondiscriminatory terms. State commissions should have the

---

[8] A.A.C. R14-2-1112, "Interconnection Requirements," provides in pertinent part, as follows:

> All local exchange carriers must provide appropriate interconnection arrangements with other telecommunications companies at reasonable prices and under reasonable terms and conditions that do not discriminate against or in favor of any provider, including the local exchange carrier. * * * The interconnection arrangements must be in the form of a tariff and shall be filed with the Commission for its approval before becoming effective.

Adopted effective June 27, 1995.

[9] Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, CC Docket No. 96-98, *First Report and Order*, 11 FCC RR-1B, CD 15499 at Section 3 (1996) (the "*Local Competition Order*").

[10] Id., at Section 4.

[11] Id., at Section 167.

> opportunity to review all agreements, including those that were negotiated before the new law was enacted, to ensure that such agreements do not discriminate against third parties, and are not contrary to the public interest. In particular, preexisting agreements may include provisions that violate or are inconsistent with the pro-competitive goals of the 1996 Act, and states may elect to reject such agreements under section 252(e)(2)(A). Requiring all contracts to be filed also limits an incumbent LEC's ability to discriminate among carriers, for at least two reasons. First, requiring public filing of agreements enables carriers to have information about rates, terms, and conditions that an incumbent LEC makes available to others. Second, any interconnection, service or network element provided under an agreement approved by the state commission under section 252 must be made available to any other requesting telecommunications carrier upon the same terms and conditions, in accordance with section 252(i). In addition, we believe that having the opportunity to review existing agreements may provide state commissions and potential competitors with a starting point for determining what is "technically feasible" for interconnection.[12]

The FCC's interpretation of § 252 to require the filing of all interconnection agreements is consistent with the clear language of § 252(e)(1), which provides, "Any interconnection agreement adopted by negotiation or arbitration shall be submitted for approval to the State commission." To the extent the Commission finds that Congress did not expressly address the question of whether interconnection agreements need be filed despite the language of § 252(e)(1), the FCC's interpretation is to be accorded deference by this Commission and should not be disturbed unless it appears from the statute or the legislative history that the interpretation is not one Congress would have sanctioned. *See Chevron U. S. A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U. S. 837, 843-845 (1984).

[12] *Local Competition Order* at Section 167.

In this case, the FCC's interpretation is also wholly in line with the legislative history of the Act. In the *Conference Committee Report* on the Act, Congress made it clear that § 251(c) imposes an obligation on ILECs to "negotiate in good faith, subject to the provisions of section 252, binding agreements to provide all of the obligations imposed in new sections 252(b) and 251(c)."[13]

Explaining § 252(e) of the Act, the *Conference Committee Report* states in relevant part, "The House recedes to the Senate on new section 252(e). Agreements arrived at through voluntary negotiation or compulsory arbitration *must* be approved by the State commission under new section 252(e)."[14] (Emphasis added). The report goes on to explain, "New section 252(i) requires a local exchange carrier to make available on the same terms and conditions to any telecommunications carrier that requests it any interconnection, service, or network element that the local exchange carrier provides to any other party under an approved agreement or statement."[15]

A. THE FCC HAS DEFINED WHAT IS CONTAINED IN AN INTERCONNECTION AGREEMENT.

The term "interconnection agreement" is not specifically defined by statute. However, the FCC has provided plenty of guidance. The FCC said in its

---

[13] *Conference Committee Report of the Telecommunications Act of 1996,* H.R. Conf. Rep. No. 104-458, 104th Cong., 2d Sess. (1996).

[14] Id., at 126.

[15] Id.

Interconnection Agreement Order[16] released October 4, 2002, that the definition "directly flows from the language of the Act." In the *Interconnection Agreement Order*, the FCC confirmed that "an agreement that creates an ongoing obligation pertaining to resale, number portability, dialing parity, access to rights-of-way, reciprocal compensation, interconnection, unbundled network elements, or collocation is an interconnection agreement that must be filed pursuant to section 252(a)(1). Id. For the following reasons, the core agreements were interconnection agreements as defined by the FCC.

Agreements that address the rates that the CLEC would pay for interconnection and/or access to UNEs must be filed with the Commission under 47 U.S.C. § 252. 47 U.S.C. § 252(a) specifically refers to a "schedule of itemized charges" as being part of an interconnection agreement. Rates also must be filed as interconnection agreements to ensure that ILECs such as Qwest provide interconnection, network elements and services at rates that are non-discriminatory as required by 47 U.S.C. § 251. It is also clear that rates must be filed as part of an interconnection agreement because, to get approval to provide interLATA long distance, ILECs must demonstrate that they have a concrete and specific legal obligation, pursuant either to a Statement of Generally Accepted Terms or a

[16] In the Matter of Qwest Communications International Inc. Petition for Declaratory Ruling on the Scope of the Duty to File and Obtain Prior Approval of Negotiated Contractual Arrangements under Section 252(a)(1), WC Docket No. 02-089, *Memorandum Opinion and Order*, Released October 4, 2002, (the "*Interconnection Agreement Order*"). R-1B, CD-2, Section 8.

Commission-approved interconnection agreement, to provide interconnection, network elements and services at non-discriminatory rates. [17]

Qwest claims that it did not file the agreements identified in Joint Exhibit 1 prior to the FCC's *Memorandum Opinion and Order* because it was not required to do so under the Act. According to Qwest, there was no national standard for determining what agreements were subject to approval under the Act. RUCO 2 at p. 28. Qwest interpreted the Act to require, in the case of negotiated ILEC-CLEC agreements, prior approval "...for core matters of price and associated service descriptions for interconnection." Id. at p. 2.

1. FOUR OF THE CORE AGREEMENTS DIRECTLY ADDRESS RATES AND WERE REQUIRED TO HAVE BEEN FILED UNDER QWEST'S PRIOR INTERPRETATION.

Even Qwest does not dispute that agreements affecting rates for interconnection and associated interconnection service descriptions for interconnection, services and network elements must be filed with the Commission. Id., S-3, at 2. Provisions in four of the core agreements discussed above fall into this undisputed category, directly addressing the rates that the CLEC would pay for interconnection. Those agreements are:

[17] See Application by SBC Communications, Inc., Southwestern Bell Tel. Co., and Southwestern Bell Communications Services, Inc. d/b/a Southwestern Bell Long Distance Pursuant to Section 271 of the Telecommunications Act of 1996 To provide In-Region, InterLATA Services in Texas, Memorandum Opinion and Order, 15 FCC Rcd 18354 (2000)(SWBC Texas Order) and 47 U.S.C. §§ 271(c)(2)(A) and 271(c)(2)(B)(i) – 271(c)(2)(B)(xiii).

- Eschelon Agreement II (10% discount/refund, $13 per month per line credit for UNE-platform lines in lieu of providing accurate daily usage files)[18];
- McLeod Agreement I (the oral agreement for a purchase volume discount/refund);
- McLeod Agreement II and III to the extent these agreements were tied into the oral discount agreement and therefore affected rates.

Each of the agreements cited above changed the rates in Eschelon and/or McLeod's interconnection agreements, including those set by the Commission in lengthy cost docket proceedings. Accordingly, Qwest was required to file the term with the Commission under 47 U.S.C. §§ 252(a) and (e).

2. TWO OF THE CORE AGREEMENTS DIRECTLY ADDRESS TERMS AND CONDITIONS FOR INTERCONNECTION SERVICE AND WERE REQUIRED TO HAVE BEEN FILED UNDER QWEST'S PRIOR INTERPRETATION.

Two of the core agreements contained provisions which governed the terms and conditions of service Qwest provided to McLeod and Eschelon. They are:

- Eschelon Agreement I (quarterly executive meetings and escalation procedures to address service quality);
- McLeod Agreement I (quarterly executive meetings and escalation procedures to address service quality).

---

[18] **[BEGIN TRADE SECRET]**

[END TRADE SECRET]

These agreements provided terms that affected the terms and conditions of how Qwest would provide interconnection services to McLeod and Eschelon. Therefore, Qwest was required to file the agreements with the Commission under 47 U.S.C. §§ 252 (a) and (c).

B. THE EXISTENCE OF THE AGREEMENTS CONSTITUTES *DE FACTO* DISCRIMINATION

The mere existence of the unfiled agreements constitutes *de facto* discrimination against non-party CLECs, even if the CLEC parties to the agreements never enforced their provisions. In other words, the fact that these agreements exist and contain interconnection terms which were not filed, is discriminatory on its face because no non-party CLEC could opt-in.

Each unfiled term creates a concrete and specific legal obligation in Qwest that the CLEC party to the agreement can, if it desires, enforce in the appropriate forum[19]. No non-party CLEC operating in Arizona is in the same position even if, as Qwest claims with respect to some provisions, Qwest's "internal policy" is to provide the same level of service to those other CLECs. As a matter of fact and law, therefore, Qwest has discriminated against CLECs that are not party to the unfiled agreements simply by entering into those agreements and not making them available for other CLECs to opt into under 47 U.S.C. § 252(i).

C. QWEST STILL CANNOT DISTINQUISH CERTAIN INTERCONNECTION TERMS IT IS REQUIRED TO FILE UNDER THE ACT

[19] These agreements could also give the CLECs leverage to extract other important concessions from Qwest. Eschelon, after all, did receive $7.9 million to terminate several of its unfiled agreements with Qwest. R-1B, CD-62, deposition, exhibit RUCO 18. No other CLECs had the opportunity to receive that same benefit because no other CLECs were party to those same terms.

The FCC's *Interconnection Agreement Order* of October 4, 2002 provided a definitive standard as to what an "interconnection agreement" means under the Act. In fact, Qwest advocates that the FCC's *Interconnection Agreement Order* "renders moot the threshold question of what standard should be applied to the CLEC contracts at issue in this case." Q-2 at 7.

Nonetheless, the evidence in the record suggests that despite the clear intent of the FCC's *Interconnection Agreement Order,* there are still instances where Qwest cannot distinguish interconnection terms that it is required to file. For example, the FCC has determined that agreements addressing escalation provisions are required to be filed under the Act unless perhaps the information is made generally available to CLEC's (i.e. on the ILEC's wholesale website). S-2 at 5. Two of the core agreements in this case contain escalation terms which are different than the information concerning escalation procedures on Qwest's website. Qwest, however, considers the escalation provisions the same, since, in practice Qwest claims it treats each CLEC the same. While it is clear that there is a distinction, Qwest does not see it, thereby placing into question Qwest's future compliance with the Act.

Qwest witness, Dana Filip Crandall, senior vice-president of customer service, explained Qwest's escalation procedures with Eschelon. Q-7 at pages 10-13. In her Direct testimony, Ms. Crandall referred to a chart in the Qwest/Eschelon Implementation Plan executed on July 31, 2001 ("Implementation Plan")[20] and the

[20] Ms. Crandall was referring to the Implementation Plan with Eschelon dated 7/31/01 which was also not filed by either party at the time it was entered into. Transcript, Vol. II, at 288:9 – 289:2, RUCO – 11.

escalation procedures described on Qwest's website to represent that the escalation procedures were the same for Eschelon as they were for the other CLECs. Id. The escalation procedures described on Qwest's website and the Implementation Plan both provide for a different escalation procedure than what Qwest agreed to in the Eschelon I and McLeod IV agreements.[21] RUCO-11, attachment 2 at pages 10-11, Q-7 at 12.

In her direct testimony, Ms. Crandall never mentions the escalation procedures agreed to on November 15, 2000 in Eschelon Agreement I. Q-7. Yet Ms. Crandall was aware at the time she filed her direct testimony of the differences in the escalation procedures described in her testimony and those agreed to in Eschelon Agreement I.[22] Ms. Crandall had even pointed out these differences in the direct testimony she previously filed in Minnesota. Transcript Vol. II, at 292:14-17. The explanation for the discrepancy is that Qwest believes the escalation processes were and still are the same[23]. Transcript, Volume II at 337:8-25.

---

[21] The Implementation Plan provides for a seven-tiered escalation process with the highest level, Tier 7 providing escalation to Qwest's vice-president. RUCO 11. The web site provides for the highest level of escalation to Qwest's vice president. Q-7 at 12.

[22] Ms. Crandall was queried on this same issue in her deposition of October 26, 2002. RUCO 13, at 22:15-26:6. Ms. Crandall admitted to "some differences" in the escalation procedures in Eschelon Agreement I and Qwest's website. RUCO 13 at 25:3-19. Ms. Crandall also acknowledged receiving a copy of Richard Smith's letter of February 8, 2002 to Joseph Nacchio regarding "Level 3 Escalation". Id. at 29:11-24.

[23] Ms. Crandall explained at the hearing that from a practical prospective as well as from her perspective the same escalation procedures are available to any CLEC. Transcript, Volume II at 291:10-292:6. If Qwest truly believed that there was no difference, then it is odd, to say the least, that Qwest would have executed the McLeod/Eschelon escalation letters and not offered the same terms in writing to other CLEC's. Qwest's argument that all the other CLECs were treated the same becomes even more suspect when the only evidence of a CLEC's utilization of the Level 3 escalation term or its equivalent is the Eschelon letter sent to Joseph Nacchio from Richard Smith on February 8, 2001. R-1B, CD-62, Deposition exhibit RUCO 13.

Whatever Qwest's perspective, there is a difference between what is described in the Implementation Plan and on Qwest's website, and the escalation procedures described in Eschelon Agreement I and McLeod Agreement IV. For filing purposes, the difference is critical. The escalation procedures agreed to in the agreements qualify as interconnection terms under the *Interconnection Agreement Order* and should have been filed (even under Qwest's original understanding of its filing obligation). The publicly available provisions represented on Qwest's website may not need to be filed under the *Interconnection Agreement Order*. The fact that Qwest still does not see the difference is troubling, and is indicative of the need for this Commission to continue to monitor Qwest's future filings.

D. ONE STATE COMMISSION HAS REVIEWED FOUR OF THE CORE AGREEMENTS AND DETERMINED THAT THEY SHOULD HAVE BEEN FILED UNDER 47 U.S.C. § 252

While this case has been proceeding in Arizona, Minnesota had conducted its own proceedings to determine whether the unfiled agreements cited in Joint Exhibit 1 should have been filed in that state. Of the core agreements, the Minnesota Public Utilities Commission (the "Minnesota Commission"[24]) determined that the provisions found in Sections 2 and 3 of McLeod Agreement IV[25], McLeod Agreement I[26],

[24] The Minnesota Commission adopted the Administrative Law Judges Findings of Fact, Conclusions, Recommendation and Memorandum ("ALJ's report") in its entirety. *See Order Adopting ALJ's Report and Establishing Comment Period Regarding Remedies, Docket No. P-421/C-02-197* ("Minnesota Order"), at p. 2. The ALJ analyzed eleven written agreements and the McLeod oral agreement and determined that those agreements should have been filed with the Minnesota Commission. The Minnesota Commission agreed with the ALJ that Qwest knowingly and intentionally violated the Act because Qwest knew that it was required to file these agreements and intentionally did not. Id., at 4.

[25] See paragraphs 301 and 310 of the ALJ's report.

[26] See section 341 of the ALJ's report.

Sections 2 and 3 of Eschelon Agreement I,[27] and paragraphs 2 and 3 of Eschelon Agreement II[28] should have been filed before the Minnesota Commission. For each of those provisions, the Commission determined that Qwest knowingly and intentionally violated the Act because Qwest knew the Act required filing but intentionally did not make the required filing. *See Order Adopting ALJ's Report and Establishing Comment Period Regarding Remedies, Docket No. P-421/C-02-197*, at page 4.

E. QWEST'S FAILURE TO FILE THE CORE AGREEMENTS VIOLATED A.A.C. R-14-2-1112

A.A.C. R-14-2-1112 provides that an ILEC must "provide appropriate interconnection arrangements" with CLECs that "do not discriminate against or in favor of any provider, including the local exchange carrier." Thus, should there be a question as to whether something qualifies as an interconnection agreement, if it is an interconnection "arrangement", the Commission Rules require that it be filed for approval.

For the reasons set forth above, the core agreements between Qwest and Eschelon and Qwest and McLeod were interconnection arrangements. Qwest's failure to file the core agreements discriminated against non-party CLEC's in violation of A.A.C. R-14-2-1112.

F. QWEST'S VIOLATION OF THE ACT AND THE COMMISSION'S RULE VIOLATED A.R.S. 40-203

[27] See sections 102 and 113 of the ALJ's report.

[28] See sections 147 and 137 of the ALJ's report.

Qwest's failure to file the core agreements was intentional and deliberate in violation of the Act and the Commission's Rules. Since the core agreements were not filed, Qwest discriminated against non-party CLEC's because non-party CLEC's were not able to opt in. The core agreements, Qwest's violation of the Act and the Commission's Rules resulted in discriminatory, preferential and illegal agreements in violation of A.R.S. § 40-203.

VI. QWEST AND MCLEOD AND QWEST AND ESCHELON ENGAGED IN A SCHEME TO DEFRAUD THIS COMMISSION IN VIOLATION OF A.R.S. § 13-2310 AND A.R.S. § 13-2311.

Qwest's failure to file agreements that it was otherwise required to file was intentional and deliberate. It was part of a larger scheme that involved two of Qwest's largest wholesale customers, McLeod and Eschelon. The separate business arrangements that Qwest had with McLeod and Eschelon each had a purpose- to undermine competition while each party realized substantial financial and other benefits. In attempting to achieve their purpose, Qwest, McLeod and Eschelon violated ARS § 13-2310 and ARS § 13-2311.

A. THE STATUTES

A.R.S. § 13-2310, "Fraudulent schemes and artifices; classification; definition" provides in relevant part:

> A. Any person who, pursuant to a scheme or artifice to defraud, knowingly obtains any benefit by means of false or fraudulent pretenses, representations, promises or material omissions is guilty of a class 2 felony.
> B. Reliance on the part of any person shall not be a necessary element of the offense described in subsection A of this section.

A.R.S. § 13-2311, "Fraudulent Schemes and Practices," provides in relevant part:

> A. Notwithstanding any provision of the law to the contrary, in any matter related to the business conducted by any department or agency of this state or any political subdivision thereof, any person who, pursuant to a scheme or artifice to defraud or deceive, knowingly falsifies, conceals or covers up a material fact by any trick, scheme or device or makes or uses any false writing or document knowing such writing or document contains any false, fictitious or fraudulent statement or entry is guilty of a class 5 felony.

The Arizona Supreme Court, in *State v. Haas*, 138 Az 413, 675 P.2d, 673 (1988), required proof of the following elements to be guilty of a fraudulent scheme or artifice under ARS § 13-2310;

1. A scheme or artifice to defraud-some "plan, devise or trick" to perpetrate a fraud. *Id.*, at 419, 675 P.2d 679.

- Scheme - "a scheme is a plan while an "artifice" is an evil or artful strategy." *Id.*, at 423, 675 P2d 683.

- Fraud - something is fraudulent when it is "reasonably calculated to deceive persons of ordinary prudence or comprehension." The Supreme Court adopted a broad view of fraud noting that " ..."fraud" must be broad enough to cover all varieties made possible by boundless human ingenuity" *Id.*, at 424, 675 P.2d 684.

2. Knowing and intentional participation. Id., at 419, 675 P.2d 679.

- Knowing - person is aware that his or her conduct is of the nature or that the circumstances exist. It does not require any knowledge that the act or omission is unlawful. ARS 13-105(9)(b).

- Intentional - person's objective is to cause the result of the conduct described in the statute or to engage in the conduct. ARS 13-105 (9)(a). An intent to defraud is not necessary. *State v. Bridgeforth,* 156 Az 60, 64, 750 P. 2d 3, 7 (1988).

3. A scheme for obtaining a money or property (benefit[29]) by means of false or fraudulent pretenses, representation, promises or material omissions. (*Haas* at 419, 675 P.2d 679) *State v. Bridgeforth,* 156 Az 60, 64, 750 P. 2d 3, 7 (1988).

- Benefit - anything of value or advantage, present or prospective ARS § 13-105(2).

ARS § 13-2311, like ARS § 13-2310, was intended to be a broad remedial statute applicable to any plan, trick or device to perpetrate a fraud. *State v. Sommer,* 155 AZ 145, 147, 745 P. 2d 203, 205 (1987). Unlike ARS § 13-2310, ARS § 13-2311 does not require a finding that a benefit was received. The Arizona Court of Appeals in *Sommer* set forth the elements of ARS § 13-2311. The Court noted:

> "... the elements of ARS § 13-2311 require that a defendant knowingly falsify or conceal a material fact or use a false writing pursuant to a plan, trick or device to defraud another." *Id.*

RUCO acknowledges that the Commission does not have jurisdiction to impose criminal penalties. Nonetheless, RUCO believes that the parties' engaged in criminal conduct which the Commission can proscribe pursuant to A.R.S. § 40-203. What RUCO is suggesting is similar to this Commission's authority to enforce the Securities Act. The Commission can order individuals to cease and desist violating certain statutes found in A.R.S. Title 44 and has the option to refer the same violations to the Attorney General's Office for consideration. Here the Commission can determine the legality of the conduct under A.R.S. § 40-203 and require the parties to cease and desist from that conduct should the Commission determine it

[29] The Arizona Courts have equated property with benefit and have consistently made it an element of ARS § 13-2310. See *State v. Bridgeforth,* 156 Az 60, 64, 750 P.2d 3, 7 (1988), *State v. Cook,* 185 AZ 358, 363, 916 P. 2d 916, 1079 (1995).

was illegal for either criminal or civil reasons. The Commission can also refer it to the Attorney General's office for further consideration if it believes a crime was committed.

B. THE McLEOD AGREEMENTS

1. QWEST AND MCLEOD ENGAGED IN A PLAN WITH THE INTENT OF DECEIVING THIS COMMISSION AND OTHER CLEC'S AS TO THE TRUE NATURE OF THEIR AGREEMENT.

A "scheme" under § ARS 13-2311 merely requires a plan. *State v. Haas*, 138 Az 413, 423, 675 P.2d, 673, 683 (1988). Through a series of unfiled and confidential agreements Qwest was able to provide McLeod with preferential pricing. In return, Qwest was assured of McLeod's neutrality in § 271 proceedings. Qwest and McLeod planned to keep these terms confidential and undisclosed. The purpose of their plan was to deceive the Commission and other CLECs. *State v. Bridgeforth,* 156 Az 60, 64, 750 P.2d 3, 7 (1988).

Qwest and McLeod negotiated[30] the terms of their business arrangement through the summer and fall of 2000. The negotiations with McLeod resulted, in part, in six written agreements that the parties entered into on October 26, 2000. The key component of those agreements was the creation of a new product called UNE-Star (or UNE-M when purchased by McLeod). The UNE-Star product is a flat-rated UNE platform product that, in essence, converted McLeod resold lines directly to UNE-P. One of the six agreements McLeod and Qwest entered into on October 26 is the Fourth Amendment to their interconnection agreement in Arizona. Joint

[30] The key players who negotiated and developed the terms of the Qwest/McLeod partnership was Audrey McKenney, and Blake Fisher, McLeod's Group Vice President and Chief Planning and Development Officer.

Exhibit 1, # 23, R-1C, MDC-4A. McLeod filed the Fourth Amendment in Arizona on December 26, 2000 which publicly disclosed terms and conditions for the UNE-Star product. Two of the other written agreements are the purchase agreements between McLeod and Qwest (McLeod Agreement I and McLeod Agreement II). Another of the six agreements is the document identified as the Confidential Letter Agreement regarding escalation procedures dated October 26, 2000. Joint Exhibit 1, #19 "Amendment to Confidential Billing Settlement Agreement" dated October 26, 2000 (the "Dispute Resolution Agreement"). Joint Exhibit 1, #23. The final two agreements are billing settlement agreements that moved substantial sums of money back and forth between McLeod and Qwest.[31] Joint Exhibit 1, # 22 and # 23.

The parties also entered into an oral agreement on October 26, 2000 (McLeod Agreement I). This agreement was not filed with the Commission. In order to understand McLeod's rates, the Commission would have had to know of the oral and unfiled written agreements. The discount provisions of the oral agreement were interrelated to the purchase volume commitments set forth in Qwest and McLeod's purchase agreements (McLeod Agreement II and McLeod Agreement III). Qwest denies the existence of the oral agreement[32], but the evidence irrefutably shows that they exist.

Blake Fisher of McLeod testified under oath in a sworn affidavit and at a deposition taken by Qwest that he entered into an oral agreement with Qwest for Qwest to provide McLeod with a purchase volume discount of up to 10%. (R-1C,

[31] These agreements amend two previous unfiled settlement agreements executed on September 29, 2000. Joint Exhibit 1, # 26 and # 27.

[32] R-1C, MDC-3B at 5:18-22.

MDC 2C ¶¶ 2, 18-20 and R-1B, CD4 at 43:2-10[33]). The quid pro quo, according to Mr. Fisher, was McLeod's agreement to remain neutral in Qwest's § 271 proceedings. R-1C, MDC 2C at ¶ 24. Lori Deutmeyer, of McLeod, was responsible for collecting the discount in arrears as a refund paid by Qwest. Ms. Deutmeyer testified how she worked with Arturo Ibarra and Anthony Washington[34] at Qwest to calculate the discount amount and collect it as a refund from Qwest. R-1C, MDC-1E at ¶¶ 2-12. David Conn, a McLeod attorney, and Stacey Stewart, a McLeod employee, also confirmed the existence of the discount agreement to RUCO's consultant, Clay Deanhardt. Transcript, Volume III at 597:3-15.

The discount agreement grew out of discussions that McLeod had with US WEST about converting McLeod's resold lines to UNE-P. At that point, the parties began negotiations to create a new product that would leave McLeod's customers on the same physical telephone lines they already had but give McLeod the benefit of better pricing across US West's region. The parties, however, could not agree on acceptable pricing before the merger. Fisher Affidavit at ¶¶ 6 – 11.

After the merger, Qwest made overtures to McLeod that it wanted to improve its relationship with McLeod as a customer. McLeod and the new Qwest subsequently restarted their conversations about converting McLeod's resold Centrex lines to UNE-P lines. Fisher Affidavit at ¶ 11.

Qwest and McLeod reached an agreement on implementation and pricing for the new UNE-P product called UNE-Star. However, McLeod was not satisfied that

[33] For ease of reference, R-1B, CD-2C will be referred to hereinafter as the "Fisher Affidavit."

[34] Mr. Ibarra, at the time, was Qwest's Director of Business development, and Mr. Washington reported directly to Mr. Ibarra. R-1C, MDC-3A at 4:24-6:23.

the pricing was low enough for McLeod to keep its traffic on Qwest's network (as compared to going off-network). Fisher Affidavit at ¶12. Qwest and McLeod therefore negotiated an additional discount agreement. Id. at ¶ 13 – 14. McLeod committed to purchasing specified volumes of Qwest products under a take-or-pay agreement and Qwest agreed to provide McLeod with discounts if McLeod exceeded its take-or-pay commitments. Id., at ¶¶17, 19-20. The McLeod take-or-pay agreement is McLeod Agreement II.

The discount Qwest agreed to provide ranged from 6.5% to 10% of the total purchases made by McLeod from Qwest. The exact amount of the discount to be applied depended on the volume of purchases made by McLeod from Qwest during the applicable year. Fisher Affidavit at ¶¶ 2, 19 – 20. The discount applied to *all* products and services purchased by McLeod from Qwest inside and outside of Qwest's 14-state ILEC territory. Id. at ¶ 2.

Mr. Fisher asked Greg Casey and Audrey McKenney from Qwest to put the discount agreement in writing, but they would not do so. R-1B, CD-4 at 58:6 – 59:9. According to Mr. Fisher, Mr. Casey and Ms. McKenney were concerned that other CLECs might feel entitled to the same discount if the agreement were written and made public. Id. at 59:10 – 24.

When Mr. Fisher expressed concern over the enforceability of the oral agreement for the discount, Qwest suggested that it would enter into its own take-or-pay agreement to purchases products from McLeod. Fisher Affidavit at ¶¶ 22-23. Mr. Fisher testified that the amount of the Qwest take-or-pay commitment was calculated by applying an 8% discount factor to a projected amount of purchases by

McLeod from Qwest. Id. at ¶ 23. McLeod Agreement III is the take-or-pay agreement that McLeod entered into with Qwest to insure that McLeod would receive the discount.

As Ms. Deutmeyer explains, however, Qwest did honor the oral discount agreement for some period of time. Qwest made discount/refund payments in excess of **[BEGIN TRADE SECRET]** **[END TRADE SECRET]** to McLeod for what Qwest called the "Preferred Vendor Plan" from October 2000 through September 2001. R-1C, MDC 1E at ¶¶ 3, 5, 9-12. Ms. Deutmeyer testified that Qwest calculated the amount of the payment by applying the 10% discount factors to all purchases made by McLeod from Qwest during the relevant time period. Id. at ¶¶ 4-8.

The existence of a pricing arrangement[35] that provided preferential terms to McLeod and was unavailable to other CLECs is a material fact since the fundamental purpose of the Act, the Commission's Rules and telecommunication regulations in general, is to prevent rate discrimination. The Supreme Court in *Haas* defined fraud for purposes of ARS § 13-2311 as something that is "reasonably calculated to deceive persons of ordinary prudence or comprehension." *State v. Haas*, 138 Az 413, 424 675 P.2d, 673, 674 (1988). Qwest's attempt to circumvent the Act by confidential purchase agreements designed to hide the true nature of the parties' agreement is fraud as defined by the Supreme Court in *Haas*.

[35] Qwest denies that it offered McLeod a volume discount. Qwest has explained the 10% discount figure on as representing a "shortfall" of what Qwest owed McLeod under the take or pay agreements. R-1C, 3B at 48:24-51:25. What it is called is irrelevant. McLeod had an undisclosed preferential pricing agreement with Qwest unavailable to any non-party CLEC.

Moreover, McLeod can hardly deny that it willingly participated in the fraud. Mr. Fisher's testimony regarding the business arrangement should be given extra weight since it amounts to an admission on McLeod's behalf to the fraud committed on this Commission and the public.

2. THE DOCUMENTS INTRODUCED IN THIS CASE CONCLUSIVELY CORROBORATE BLAKE FISHER'S TESTIMONY THAT QWEST AGREED TO PROVIDE MCLEOD WITH A PURCHASE VOLUME DISCOUNT.

More than 40 documents introduced as evidence in this case either refer directly to the discount agreement or show the implementation of the agreement by Qwest. Those documents are categorized and set out in the table below:

Documents Evidencing Qwest's Oral Discount Agreement with McLeod	
Category	Document
Negotiation documents created by Qwest that show Qwest's offer of the discount terms to McLeod	R-1B, CD-19, R-1B, CD-22, R-1B, CD-23, R-1B, CD-25, R-1B, CD-26, R-1B, CD-27, R-1B, CD-28, R-1B, CD-29; Fisher Affidavit, Exhibits 2 (created jointly by Qwest and McLeod) and 3.
Negotiation documents created by McLeod that show McLeod negotiating terms of the discount with Qwest	R-1B, CD-17, R-1B, CD-21, R-1B, CD-24, R-1B, CD-32; Fisher Affidavit, Exhibit 2 (created jointly by Qwest and McLeod).
Documents created by Qwest showing its consideration of the impact of various discount proposals it generated	R-1B, CD-16, R-1B, CD-25, R-1B, CD-28, R-1B, CD-33.
Presentations made by Qwest to McLeod during the negotiation of the discount	R-1B, CD-18, R-1B, CD-19.

Documents showing calculation of the discount amounts owed by Qwest to McLeod as a refund	R-1B, CD-7, R-1B, CD-8, R-1B, CD-9, R-1B, CD-10, R-1B, CD-11, R-1B, CD-38, Deutmeyer Affidavit, Exhibit 1.
Documents showing the payment of the discount amounts owed by Qwest to McLeod as a refund	R-1B, CD-13, R-1B, CD-12, Deutmeyer Affidavit, Exhibits 2-5.
Post-agreement documents in which Qwest called the agreement a "discount" in communications with McLeod	R-1B, CD-42, R-1B, CD-50, R-1B, CD-53.
Post-agreement documents in which McLeod called the agreement a "discount" (or a credit or other synonymous term) in communications with Qwest	R-1B, CD-R-1B, CD-41, R-1B, CD-42, R-1B, CD-43, R-1B, CD-44, R-1B, CD-46, R-1B, CD-47, R-1B, CD-48.
Handwritten notes by Qwest's senior vice-president of wholesale markets, Audrey McKenney referring to the discount	R-1B, CD-34, R-1B, CD-39, R-1B, CD-47.
Post-agreement documents generated internally by McLeod, but not sent to Qwest, that refer to the discount	R-1B, CD-56, R-1B, CD-57, Fisher Affidavit, Exhibit 4.
Post-agreement documents showing McLeod and Qwest negotiating additional discount levels as part of follow-on discussions that never resulted in an agreement	R-1B, CD-46, R-1B, CD-47, R-1B, CD-48, R-1B, CD-49, R-1B, CD-50.

The documents described in more detail below are representative of the evidence set out in the table.

- Exhibit 2 to Mr. Fisher's affidavit is a true copy of a September 19, 2000 term sheet describing the terms of the deal being negotiated by McLeod and Qwest. Fisher Affidavit at ¶ 25. Mr. Fisher testified that the parties created the term sheet together. Fisher Affidavit at ¶ 25, Exhibit R-1B, CD-18 is another copy of the same document that came from Ms. McKenney's files. Item number 6 reads: "Based on the proposed commitment by M, within 5 business days, Q will propose volume and term discounts based on quarterly revenue targets, to be paid back to M by Q on a quarterly basis."
- Exhibits R-1B, CD-23, R-1B, CD-26, R-1B, CD-27, R-1B, CD-29 and Exhibit 3 to the Fisher Affidavit are all copies of Qwest counteroffers for discounts sent by Qwest to McLeod on October 20, 21 and 22, 2000, during the final negotiations of the discount amount.
- Exhibit R-1B, CD-50 is an e-mail dated June 13, 2001, from Arturo Ibarra, one of Qwest employees who was involved in the discount agreement negotiations. R-1C, MDC-3B at 7:14-21. Mr. Ibarra refers to the document introduced as R-1B, CD-29 as "the documentation on our 10/22/00 weekend proposals" to which both parties had agreed. (*See also* Fisher Affidavit at ¶¶19, 26 and Exhibit 3). Note that R-1B, CD-29 refers to the "Discount Rate" to be provided from "Qwest to McLeod" and the minimum purchases by McLeod required for the discount rates to apply. The discount rates and minimum purchase amounts set out in R-1B, CD-29 are identical to both the deal described by McLeod's Mr. Balvanz in the

document attached as Exhibit 4 to the Fisher Affidavit and the deal testified to by Mr. Fisher. Fisher Affidavit at ¶ 27.

- R-1C, MDC-1A is a copy of the April 2001 through June 2001 spreadsheets Qwest used to calculate the amount of the discount due to be paid as a refund to McLeod. R-1C, MDC-1B is copies of the invoices McLeod sent to Qwest and R-1C, MDC-1C is copies of the Qwest authorizations for payment. In each case, Qwest calculated the amounts owed to McLeod by multiplying the dollar amount of McLeod purchases from Qwest by 10% in accord with the discount agreement. *See* R-1C, MDC-1E, ¶¶ 6 and 7.
- Trial Exhibits R-1C, MDC-3C contain memoranda drafted by Mr. Ibarra, instructing Qwest's accounting department to "reduce UNE-Star revenues for the 10% discount that will be issued to Eschelon and McLeod should they meet they're [sic] revenue/volume commitments per the UNE-Star contract." These memoranda were created in March and April 2001.
- R-1B, CD-47 is a printout of a proposal made by McLeod in May 2001, to extend the terms of the discount agreement to include an additional year and an additional discount tier. (*See* R-1B, CD-46). Ms. McKenney wrote "Today's contract" in the margin of page 2 of R-1B, CD-47 corresponding to the deal described in R-1B, CD-29.
- R-1B, CD-53 contains a proposal letter sent by e-mail from Qwest to McLeod on June 11, 2001 during negotiations for a reduction in the price of ISDN-PRI circuits purchased by McLeod from Qwest. Ms. McKenney

and Jim Shearburn, a Qwest Regional Vice-President for Wholesale Sales wrote the letter for signature, and the transmittal e-mail was copied to Ms. McKenney. The letter says the following on page 3 under the heading "Approved Rates": "4) Please note 'NO' Additional Reseller Discounts Apply to the **[BEGIN TRADE SECRET] [END TRADE SECRET]** price. The rate for McLeod's ISDN/PRI services stated in this contract does not apply to any other discounts and specifically, that the 10% Business to Business reduction does not apply to the services addressed in this Contract."

- R-1B, CD-55 is a June 18, 2001 e-mail circulated only within Qwest in which Mr. Shearburn writes, "Audrey needs to come up with alternate language dealing with the 10% B2B deal. We should not use the language we have in the proposal, too specific. We either use the alternate language, or reprice all components at a rate 10% higher, and remove the paragraph entirely."

Mr. Deanhardt testified that the pre-agreement documents cited above are consistent with the exchange of documents one would expect to see in a heavily negotiated agreement. R-1B at 36:1-3. The post-agreement documents also are important because they show Qwest taking into account the 10% discount as it negotiated new agreements with McLeod. R-1B at 43:21-44:2. These documents disprove Qwest's explanations that no one at Qwest or McLeod other than Mrs. McKenney understood the agreements. These are documents that Ms. McKenney either reviewed or wrote, and they clearly demonstrate that Qwest and McLeod had

a mutual understanding regarding the existence of the discount agreements. Id., at 44:6-13.

In stark contrast to the myriad of references to the discount agreement documents created by Qwest, there is not a single document in evidence in which Qwest tells McLeod during the October 2000 negotiations that Qwest will not enter into a discount agreement. Neither is there a single document in evidence dated after the October 2000 negotiations in which Qwest tells McLeod that there is no discount agreement. Id. at 44:3-4.

Amendment No. 4 to the Interconnection agreement was the only filed agreement executed by the parties on October 26, 2000 that disclosed terms and conditions of the UNE-Star product. Without knowledge of the terms and conditions in the unfiled agreements of October 26, 2000 neither the Commission or the public would have been aware of the true nature of the parties relationship. The overwhelming evidence in this record shows that Qwest and McLeod participated in this scheme to misrepresent to the Commission and the public the true nature of their business relationship.

3. QWEST AND MCLEOD KNEW THAT THE AGREEMENTS SHOULD HAVE BEEN FILED WITH THE COMMISSION, BUT INTENTIONALLY CHOSE NOT TO FILE THEM.

Both Qwest and McLeod knew the nature of their conduct and that their conduct would result in the non-disclosure of their business arrangement. Their objective was to keep other CLECs from opting in to their agreement.

McLeod, even though it was not obligated by the Act to file interconnection agreements, agreed to not put the key terms of its business arrangement in writing.

McLeod knew these terms were not going to be filed. Moreover, McLeod assisted Qwest in misrepresenting the business arrangement by only filing one agreement, which alone did not represent the true nature of the parties' business relationship.

As discussed more thoroughly above, Qwest went to great pains to conceal its discount agreements with McLeod. Mr. Fisher, in fact, explained that the single reason given by Qwest for not wanting to put the discount agreement in writing was because other CLECs might feel entitled to opt into the agreement. R-1B, CD-4 at 58:6 – 59:24.

The agreements the parties entered into contained confidentiality provisions, and the evidence shows that Qwest requested the confidentiality provisions. The agreements themselves therefore evidence Qwest's intent not to file the core agreements. A major motive for doing so was to prevent other carriers from opting into the agreements, which establishes that Qwest was intentionally engaged in a pattern of discrimination against the non-party carriers. R-1B, CD-4 at 58:6 – 59:24.

Moreover, the discount agreement should have been filed, even under Qwest's interpretation of the filing requirements proposed in its petition for declaratory relief to the FCC. As the FCC pointed out in its Interconnection Agreement Order, "Qwest contends that a negotiated agreement should be filed for state commission approval if it includes: (i) a description of the service or network element being offered; (ii) the various options available to the requesting carrier (*e.g.,* loop capacities) and any binding contractual commitments regarding the quality or performance of the service or network element; and (iii) the rate structures and rate levels associated with each such option (*e.g.,* recurring and nonrecurring

charges, volume or term commitments)." Qwest cannot deny that the discount agreement addressed the "rate structure and rate levels associated with" the UNEs and services it sold McLeod, including "volume or term commitments." R-1B at 49:15-50:3.

McLeod was also aware that the agreements needed to be filed with the Commission. Randy Rings, a McLeod attorney, made this clear in the draft "interconnection agreement" he prepared. R-1B at 30:18-19. His reference to placing discount terms in a "side letter" and modifying language to avoid "pick and choose" are undisputable proof that the parties were aware of the Act's filing requirements. They also show, indisputably, that a paramount concern of the parties was to avoid making these terms available to other CLECs. R-1B at 50:4-6, CD-32.

Further evidence that McLeod was aware of the need to file the agreements is a March 1, 2001 e-mail from Jim Balvanz, Vice-President of Finance at McLeod to Gary Dupler, at the time a Vice President of Network Planning at McLeod. Mr. Dupler asked Mr. Balvanz a series of questions about the discount agreement. In one response to a question asking how McLeod knew the discount has been applied to new services, Mr. Balvanz wrote "the line people @ Qwest shouldn't know. – Greg Casey knows, but he said "w/sle group will give McLD "best available pricing" - Confidentiality is stressed BY Q – not be in any contracts." R-1C, MDC-2C, deposition exhibit 4, R-1B at 14:12-13, 42:7-8. This evidence is corroborated by Mr. Fisher's testimony that Mr. Casey and Ms. McKenney specifically told him that McLeod's discount had to remain unwritten. R-1B, CD-4 at 58:6 – 59:24.

The most compelling evidence of McLeod's intent, knowledge and complicity in the scheme is the unfiled agreements themselves. McLeod was aware of Qwest's intent when it agreed to Qwest's proposal on how to structure the discount in a way that was obviously calculated to deceive other CLECs as well as the Commission. McLeod signed the agreements knowing that they were not representative of Qwest and McLeod's business arrangement. Finally, McLeod filed one agreement, the Fourth Amendment, even though it was not required to. McLeod knew that, standing alone, the Fourth Amendment did not represent the full extent of the parties' agreement.

4. QWEST AND MCLEOD BENEFITTED FROM THEIR SCHEME

Qwest and McLeod benefited significantly from their scheme. Other than Eschelon, no other CLEC enjoyed volume discounts on their purchases. McLeod received in excess of **[BEGIN TRADE SECRET]** **[END TRADE SECRET]** in discounts. R-1C, MDC-1E, at ¶¶ 3, 5, 9-12.

McLeod was able to move to a new pricing platform (UNE-Star) without having to convert its old platform (Centrex) to a new platform (UNE-P). This spared McLeod the operational and administrative difficulties which follow conversion to a UNE-P platform. Transcript, Volume III at 606:15 – 607:1.

Another benefit that McLeod received, as more fully discussed in section V(A)(2) and V(D) above, was a preferential escalation procedure enjoyed by only one other CLEC-Eschelon. McLeod's escalation agreement allowed escalation of disputes to Qwest's CEO. McLeod Agreement I. Access to the ILEC's CEO

through a written escalation procedure could be an enormous benefit. Transcript, Volume III at 607:24 –608:12.

Qwest also benefited significantly. Primarily, Qwest was able to neutralize some of its opposition to its § 271 processes. This was significant since McLeod was experiencing service related problems during 2000 and 2001 that Qwest would have preferred were not raised as a part of the § 271 process. R-1C, CD-44.

Qwest's other benefit in keeping the deal secret was that the discount was not available to other CLECs. Hence, Qwest avoided decreased revenues that would result if other CLECs had received the same pricing opportunities. Transcript, Volume III at 611:2-12.

Qwest was also able to keep one of its larger wholesale customers on its network. Qwest had a significant financial benefit in assuring that McLeod remained on its network. R-1B at 46:16-21. Of further benefit to Qwest was McLeod's guarantee of a minimum amount of purchases. **[BEGIN TRADE SECRET]**

[END TRADE SECRET]

C. THE ESCHELON AGREEMENTS

1. QWEST AND ESCHELON ENGAGED IN A PLAN WITH THE INTENT OF DECEIVING THIS COMMISSION AND OTHER CLEC's AS TO THE TRUE NATURE OF THEIR AGREEMENT.

At about the same time Qwest entered into the volume discount agreement with McLeod it entered into another discount agreement with Eschelon. The objective was the same (preferential pricing in exchange for Eschelon's neutrality in

the § 271 process) but the plan was different. The Eschelon discount agreement was written, but was hidden in a sham "consulting" arrangement that is set out in Paragraph 3 of Eschelon Agreement II. Under that agreement, Qwest was required to rebate to Eschelon 10% of all Eschelon's aggregate purchases between November 15, 2000 and December 31, 2005, so long as Eschelon met certain minimum purchase commitments. R-1C, MDC-5A.

A November 5, 2000 letter from Eschelon's president, Richard Smith to Jim Gallegos, Judy Tinkham and Audrey McKenney at Qwest[36] evidences the fact that the consulting arrangement was intended to evade regulatory scrutiny. R-1B, CD-63. According to numbered paragraph 1, Qwest agreed to provide Eschelon with a volume discount equal to 10% of its purchases from Qwest.[37] The parties next considered how to implement their plan. Qwest was concerned with what it considered were unfair or overbroad opt-in provisions. S-13 at 2, footnote 3. Qwest suggested an oral pricing agreement but Eschelon objected. Id. Mr. Smith noted in paragraph 7 of the November 5, 2000 letter that he had an idea how to enter into the agreement with a "mechanism that makes it more difficult for any party to opt into

[36] Mr. Gallegos was Qwest's Corporate Counsel, Ms. Tinkham was Qwest's Vice President – Wholesale and Diversified Markets, and Ms. McKenney was Qwest's Vice President – Wholesale Markets Finance.

[37] Qwest made this agreement on October 21, 2000 - only five days before the series of agreements entered into by Qwest and McLeod that includes the oral volume discount agreement. It is also the same day that Qwest made the discount proposal to McLeod that is found in Exhibit 3 to the Fisher Affidavit.

our agreements."[38] R-1B, CD-63. Eschelon suggested a "...legitimate mechanism for Qwest to purchase valid consulting services from Eschelon to be reflected in a written agreement." S-13 at 2, footnote 3. Qwest adopted Mr. Smith's idea, when ten days later, it entered into Eschelon Agreement II containing Qwest's agreement to give Eschelon a 10% refund on all of its purchases from Qwest in exchange for "consulting" services.

R-1B, CD-64 and R-1B, CD-65 further evidence the existence of the discount agreement. R-1B, CD-64 is an August 28, 2000 presentation created by Qwest entitled "Revenue Commitment Incentive Plan." Under the "Overview" on page 4, Qwest noted that there would be an "Additional discount for Take or Pay multi-year commitment" and a "Year end rebate based on recurring billing."

R-1B, CD-65 is an October 14, 2000 letter sent by Richard Smith of Eschelon to Audrey McKenney at Qwest. The letter begins: "This memorandum outlines the Unbundled Network Element Platform (UNE-P) Term Purchase Agreement reached between representatives of Qwest and Eschelon on Thursday, October 12, 2000 in Denver, Colorado." On page 2, Mr. Smith writes, "Eschelon will commit to spending $100M for all Qwest services over a five (5) year term in exchange for a 15% discount off the base prices." The letter also sets out UNE-P prices "with" and "without" the volume discount.

[38] In fairness to Eschelon, Eschelon claims that Mr. Smith's use of the "opt-in" term shows that Mr. Smith "...envisioned at the time that, although more difficult to adopt because of the condition imposed by Qwest, the term may be available to other CLECs." S-13 at 2, footnote 3. Eschelon's explanation of Mr. Smith's concern for the availability of these terms to other CLECs must be weighed against Mr. Smith's deposition testimony wherein he stated that he did not "care" that other CLECs would not get the same terms as Eschelon was getting. R-1B, CD-62 at 43:24-44:2.

While the final discount terms in Eschelon Agreement II differ from those in R-1B, CD-65, both it and R-1B, CD-64 support the accuracy of Mr. Smith's November 5, 2000 letter. The evidence is overwhelming that the parties agreed to a volume discount prior to executing Eschelon Agreement II. The consulting agreement, like the McLeod Purchase Agreements, was merely a cover to hide the party's true business arrangement. The plan was carefully crafted to misrepresent to anyone reviewing it the true nature of the parties' business relationship.

In the event there is any remaining doubt as to the legitimacy of the consulting agreement, the most compelling evidence that it was a sham are the terms themselves. Eschelon Agreement II ties Eschelon's "compensation" only to the amount of its purchases from Qwest. In other words, the payment had no rational relationship to the amount or value of the "consulting" services actually performed by Eschelon. In fact, the agreement provides that if Eschelon did not meet the purchase commitment described in Confidential Purchase Agreement (R-1C, MDC-5A), then every penny of the discount would go back to Qwest regardless of how much work Eschelon actually did for Qwest. Likewise, if Eschelon purchased more than the $150 million purchase agreement amount, it would still get 10% off of the excess purchases. So, for example, if Eschelon purchased $500 million of "products" from Qwest during the term of the agreement, then Eschelon would receive a $50 million discount / refund under the agreement even if it did absolutely nothing else for Qwest under the agreement. R-1B at 58:9-20.

Moreover, Mr. Deanhardt found no evidence that any of the documents one would normally expect to see in a real consulting relationship – documents like time

records – ever existed with respect to this relationship. Mr. Deanhardt reviewed all of the documents produced by Eschelon and Qwest to RUCO, including all of the documents in Qwest's position demonstrating the work done by Eschelon under the "consulting" agreement. R-1B at 59:4-14. The "consulting" work Qwest claims was the basis for its payments to Eschelon was no different than the work other CLECs do all the time to improve the quality of the products and services they purchase. Id. In fact, as Mr. Deanhardt explained, the work that Eschelon did with Qwest is almost identical to the work done by CLECs that worked to implement line sharing for the first time in the United States. Id. None of the participants were paid for that work, nor would they have expected to be paid. Id. The simple reality was that Eschelon was paid for services that other CLECs would have happily done at no cost in the hope of getting better service. Id.

Additional evidence proving the sham includes Eschelon's statements regarding Qwest's failure to honor the terms of the consulting agreement. Eschelon claims that there is extensive documentation showing its efforts to honor the terms of the consulting agreement. Despite Eschelon's efforts, Eschelon claims that Qwest treated the consulting agreement as a "sham almost immediately." S-13 at 3, footnote 3. Eschelon noted that Qwest's immediate failure to honor the terms of the consulting agreement showed its true intent and purpose in making the agreement. Id. Qwest's intent and purpose, as even suggested by Eschelon, was to deceive this Commission and other non-party CLECs as to the true nature of its agreement with Eschelon.

Finally, the Minnesota Public Utilities Commission found that the consulting arrangement was a sham. ALJ's Findings paragraph 126.

In truth, the only possible explanation for the compensation arrangement in Eschelon Agreement II is that it was a purchase volume discount as described in Mr. Smith's November 5, 2000 letter. The parties agreed on a mechanism that at the very least would make it more difficult for other CLECs to opt-into. The parties' agreement was calculated to frustrate the fundamental purpose behind the federal laws and the Commission's Rules.

2. QWEST AND ESCHELON KNEW THAT THE AGREEMENTS SHOULD HAVE BEEN FILED WITH THE COMMISSION, BUT INTENTIONALLY CHOSE NOT TO FILE THEM.

Both Qwest and Eschelon knew the nature of their conduct and that their conduct would result in the non-disclosure of their business arrangement. Their objective was to keep other CLECs from opting in to their agreement.

Eschelon agreed to the fraudulent[39] pricing scheme knowing that Qwest was not going to disclose the terms. Eschelon's involvement was more than just its knowledge. Like McLeod, Eschelon assisted Qwest in misrepresenting the business arrangement. The most compelling example of Eschelon's assistance was its filing with this Commission of the Seventh Amendment knowing that this one agreement, filed alone, misrepresented the true nature of the parties agreement.

[39] Eschelon claims the discount agreement was legitimate at the time it was entered into. S-13 at 3, footnote 3. Even if that were the case, it is a moot point since Eschelon knew that Qwest was not going to file the discount agreement. Moreover, Eschelon admitted that Qwest began to treat the consulting agreement as a sham almost immediately, yet Eschelon still did not disclose to the Commission the terms of the Agreement. Id., at 3. Eschelon's belief, if true, makes it no less culpable for its acts.

R-1B, CD-62, deposition exhibit RUCO 5 is conclusive proof that Eschelon knew that the discount agreement that they entered into with Qwest was not going to be filed. R-1B, CD-62, deposition exhibit RUCO 5 is an internal memo from Richard Smith to various employees at Eschelon. R-1B, CD-62 at 50:12-16. In that memo, Mr. Smith identifies the five agreements executed on November 15, 2000. Under the confidential heading, Mr. Smith identifies Eschelon Agreement I and Eschelon Agreement II. R-1B, CD-62, deposition exhibit RUCO 5. Only one agreement, the Seventh Amendment (Interconnection Agreement Amendment Terms) was listed under the public heading. Eschelon clearly knew and acquiesced to the misrepresentation of the discount agreement to the Commission.

Qwest also intended to make sure the plan remained confidential. Popp Communications, another CLEC, inquired in December 2000 into the UNE-Star agreement that Qwest had with Eschelon. R-1B at 61:1-16. Qwest could not explain to Popp why Eschelon would have purchased the UNE-Star based on $10,000,000 up front conversion costs that Popp had reviewed in the publicly filed agreement.[40] Id., R-1B, CD-75. Qwest could not make the explanation because of the confidentiality of "other non disclosed reasons". Id. Despite those reasons, Qwest was not disclosing terms that it was providing to another CLEC.

Another example highlighting Qwest's intent to keep its agreement with Eschelon confidential involved an e-mail written by Laurie Korneffel, an attorney for Qwest, and sent to Jeff Oxley, an attorney for Eschelon, on April 26, 2001. R-1B, CD-70. The purpose of the e-mail was, in part, to discuss how Qwest and Eschelon

[40] Popp was referring to the Interconnection Agreement Amendment filed in Minnesota which in substance was the same as the Seventh Amendment filed in Arizona. R-1B, CD-62, deposition exhibit RUCO 8.

were going to amend portions of the implementation plan and the escalation procedures letter. Eschelon had proposed making the amendments in one letter, but Qwest wanted to make the amendments in separate letters because Qwest thought the escalation letter was "most likely to be subject to disclosure down the road." R-1B, CD-70.

Qwest's intent to maintain confidentiality regarding the escalation provisions dates back to the negotiations preceding the execution of the November 15, 2000 escalation letter. For example, R-1B, CD-68 and R-1B, CD-69 are e-mails exchanged between Laurie Korneffel, an attorney at Qwest, and Karen Clauson at Eschelon. In R-1B, CD-68, Ms. Korneffel sent a draft agreement to Mr. Oxley. The draft contains the phrase "and the Interconnection Agreements are hereby amended accordingly" at the end of section 3. Ms. Clauson, who responded on Mr. Oxley's behalf, suggested that Ms. Korneffel should remove the phrase because "this would defeat the confidentiality of the letter." As Ms. Clauson explains, "the MN PUC has specifically ordered that amendments must be filed with, and approved by, the PUC. In any event, this would be the result under the Act." R-1B, CD-69. The phrase was omitted from the final version of the agreement. Mrs. Clauson's comments show her knowledge of Qwest's intent to keep it confidential, and her willingness to assist Qwest in carrying out the plan.

Further, on March 1, 2002 Qwest entered into a "Settlement Agreement" with Eschelon. R-1B, CD-62, deposition exhibit RUCO-18. In the agreement, Qwest agreed to pay Eschelon $7,912,000 in exchange for, among other things, the immediate termination of eight Eschelon agreements, including Eschelon Agreement

I and Eschelon Agreement II. Qwest's termination of these agreements just over two weeks after the Minnesota Department of Commerce filed its 252 complaint with the Minnesota Public Utility Commission on February 14, 2001[41] was another attempt to prevent CLECs from being able to opt into their provisions – in particular the 10% refund Eschelon received on all of its purchases from Qwest. Qwest's immediate termination of these agreements after the Minnesota 252 proceeding was initiated further evidences Qwest's knowledge and intent to not to make the agreement terms available to other CLECs in violation of 47 U.S.C. § 251.

3. QWEST AND ESCHELON BENEFITTED FROM THEIR SCHEME

Each party derived substantial benefits from their agreement. Eschelon received in excess of $3.6 million in discounts. R-1C at 5:14. Qwest was assured of Eschelon's neutrality in the § 271 proceedings.

The parties benefited in same ways as the parties did in the Qwest/McLeod business arrangement described in section (B)(4) above. As with McLeod, Qwest and Eschelon's business relationship continued to worsen after they executed their agreement on November 15, 2000. Eschelon went to great lengths to remedy the situation, leaving behind a document trail establishing how truly deceitful the business arrangement was. Mr. Smith describes in detail the benefits of Qwest and Eschelon's business relationship in an e-mail sent to Qwest on October 8, 2001. R-1B, CD-72. Mr. Smith emphasized Eschelon's efforts to covertly assist Qwest before state commissions. Mr. Smith notes that Eschelon had provided favorable testimony in § 271 workshops dealing with Qwest's Performance Assurance Plan.

[41] See ALJ's Report, paragraph 31.

At the same time Eschelon had not made its Report Card of Qwest's unsatisfactory performance available to other carriers or regulatory commissions. Nor had Eschelon disclosed any of the problems it was experiencing with Qwest's access billing records[42] or general billings for UNEs and UNE-E lines. R-1B, CD-72.

D. QWEST AND ESCHELON AND QWEST AND MCLEODS' SCHEMES TO DEFRAUD THIS COMMISSION VIOLATED A.R.S. § 40-203

Qwest and Eschelon and Qwest and McLeod knew the nature of their conduct and knew their conduct would result in the non-disclosure of their agreements. Moreover, non-disclosure was their intent. They each benefited, as described above, by not disclosing the terms of their agreements. Their schemes to defraud this Commission were successful and were discriminatory, preferential and illegal practices in violation of A.R.S. § 40-203.

VII. REMEDIES

In this proceeding, neither Qwest, Eschelon nor McLeod has offered credible evidence to refute the accusations that they violated the law. Neither Eschelon nor McLeod filed testimony in this proceeding or called a single witness at the hearing. Qwest has filed testimony claiming as a defense that it misinterpreted the law, but did not file testimony or offer one witness at trial who negotiated the core terms

[42] In a letter to Mr. Nacchio, Qwest's CEO, of November 8, 2002, Mr. Smith described the on-going access dispute between Eschelon and Qwest. Although the dispute appears to have been resolved in Eschelon's favor by an audit, Qwest went to great lengths to make sure that the audit results were not disclosed. Qwest sought Eschelon's agreement requiring Eschelon to turn over all the audit documents to Qwest and to provide favorable testimony in a manner suitable to Qwest in proceedings before regulatory commissions. R-1B, CD-62, deposition exhibit RUCO 13 at 5, S-15, S-16.

which are the subject of this proceeding[43].

Rather, Qwest has tried to put into "context" its past noncompliance and address remedies for violations that, if true, Qwest's claims would have had no impact on competition. In fact, Qwest goes so far as saying that consumers actually benefit where Qwest provides an undisclosed discount to a CLEC.[44] Furthermore, Qwest still believes that the § 271 process was not harmed by the non-participation agreements. Q-13 at 19:16-18. It should come as no surprise that Qwest recommends "modest" penalties in this case. Id. at 21:3.

1. THE IMPACT ON COMPETITION AND THE § 271 PROCESS

Qwest's agreement to provide purchase volume discounts to Eschelon and McLeod but to no other CLECs constituted illegal rate discrimination against every other CLEC operating in Arizona. The evidence discussed above shows that both McLeod and Eschelon received 10% discounts during 2000 and 2001 on every purchase they made from Qwest, including their purchase of UNEs, tariffed services, switched access and other telecommunications services covered by the Act.

These discounts gave Eschelon and McLeod enormous pricing and operational advantages *vis a vis* other CLECs that did not have an opportunity to obtain the same discount. R-1B at 12-68. Every CLEC that did not have this 10% discount suffered the direct harm of paying more for interconnection, network elements and services than the law requires. That directly affects each CLEC's bottom line by reducing the net between revenues and expenses. To many CLEC's

[43] Judith Rixe was present at the negotiations but her role was as customer advocate, not negotiator. Ms. Rixe "sat at the side" during the negotiations. Transcript, Vol. II at 367:1-11.

[44] According to Qwest, the discount forces other CLECs to lower their prices benefiting the consumer. Q-13 at 18:12-16.

who are struggling to survive in the currently troubled telecommunications market, reductions to their bottom line can be devastating.

The impact of this discrimination cannot be underestimated. The evidence shows that Eschelon received $3.6 million in discounts and McLeod received **[BEGIN TRADE SECRET]** **[END TRADE SECRET]** in refund payments. R-1C at 3:14, 5:8-9. Moreover, the application of the discount to amounts spent by other CLECs in Arizona alone would have amounted to millions of dollars in refunds for the CLECs operating here, and millions more for those CLECs that also operate in other states.

Qwest's conduct in terminating several of the most beneficial Eschelon agreements in an attempt to prevent their terms from becoming publicly available for other CLECs to adopt is an admission of culpability. It is also a slap in the face to the authority of the Commission to rectify the wrongs committed by Qwest.

Perhaps more disturbing is Qwest's argument that there was no harm caused by the non-participation agreements that Qwest had with McLeod and Eschelon. Given the enormity of this proceeding and the § 271 proceeding, it is easy to lose sight of the big picture. For competition to have a chance, the Commission must be allowed to do its job to ensure that Qwest is not permitted to use its superior market power against its competitors. The Commission has been engaged in the § 271 process for the past four years. For the most part, this Commission has been approving the necessary checklist items mandated by the Act. While Qwest was making its case and assuring this Commission that it was in compliance with the various checklist items required by the Act, it had been, and still appears to be,

embroiled in a bitter dispute with Eschelon regarding, primarily, service related issues. R-1B, CD-62, deposition exhibit RUCO 12. McLeod has also experienced significant service related problems with Qwest after it entered into the non-participation clauses[45]. R-1B, CD-44.

These service-related issues were not made a part of the § 271 record because of the non-participation clauses. Therefore, these issues were not discussed or considered in the forum where all the CLECs could have participated. One of the main purposes for the collaborative approach the Commission has taken for the § 271 process is to consider service related issues and establish processes for the implementation of any resolutions on a CLEC-wide basis. The non-participation clauses allowed Qwest to limit what issues were to be considered in the § 271 process. It also allowed Qwest to control the resolution of those disputes it had with Eschelon and McLeod without fear that the resolutions would be applied to all CLECs. Qwest did this while at the same time representing to the Commission that it was in compliance.

Qwest's actions, as well as its representations to this Commission, tainted the integrity of the § 271 process. There is ample evidence in this record that Qwest not only tried to neutralize Eschelon[46] but that Qwest required as a condition to dispute resolutions that Eschelon would provide favorable testimony in a manner suitable to Qwest in regulatory proceedings. See S-15, R-1B, CD-62 deposition exhibit RUCO

[45] Non-participation clause refers to the party CLEC's agreement with Qwest to remain neutral in Qwest's § 271 proceedings.

[46] Qwest and McLeod also negotiated dispute resolution terms which involved McLeod's support for Qwest in its 271 application. R-1B, CD-46, 47, and 48.

13. The notion of a "paid witness" is offensive and suggests that Qwest has turned the § 271 proceeding into a sham.

The fact that Qwest would resort to adhesion to sequester favorable testimony allows this Commission to better understand Qwest's corporate culture. Unfortunately, Qwest did not understand the negative impact of its actions on the § 271 process before, or does it now; otherwise it would not be advocating that there was no impact on the § 271 process.

In addition, Qwest's agreement to give discounts without the Commission's knowledge undermines the Commission's exclusive authority to set rates. In Arizona, the Constitution empowers the Commission, not Qwest, with ratemaking powers. Qwest's usurpation of this Commission's power was not only bad judgment, it was intentional. It is also indicative of Qwest's complete lack of respect for this Commission's authority. Qwest's conduct in terminating several of the most beneficial Eschelon agreements in an attempt to prevent their terms from becoming publicly available for other CLECs to adopt is another slap in the face to the authority of the Commission to rectify the wrongs committed by Qwest.

The Commission must consider serious and far-reaching remedies. The Commission must send a signal to Qwest, Eschelon and McLeod that their corporate cultures must change and that their past conduct will not be tolerated in Arizona in the future.

2. SUBSTANTIAL PENALTIES SHOULD BE ASSESSED AGAINST QWEST, ESCHELON AND MCLEOD.

In the end, there is almost nothing the Commission could do to effectively redress the harm that the parties' conduct has caused to other Arizona CLECs, the competitive landscape and the regulatory environment in Arizona. However, based on the record in this case RUCO respectfully requests that the Commission (a) establish a two-part fund to facilitate arbitrations between Qwest[47] and the CLECs; (b) request Qwest to provide CLECs with rebates or bill credits to compensate for poor service quality; (c) order Qwest to offer a 10% discount off its UNE prices for the same length of time the 10% discount had been offered to Eschelon and McLeod; (d) require Qwest to accelerate its deployment of broadband facilities; and (e) order Eschelon and McLeod to contribute at least $100,000 each to the two-part fund.

A. RUCO'S RECOMMENDATIONS ARE REASONABLE AND APPROPRIATE UNDER THE CIRCUMSTANCES OF THIS CASE

The record in this matter requires that substantial penalties be assessed against Qwest, Eschelon and McLeod for willfully and intentionally misrepresenting their agreements and for discriminating against other CLECs by not making those provisions available to them. Because of the far reaching impact that the parties conduct had on competition in Arizona, as well as on the integrity of the process, RUCO concentrated its remedy analysis on equitable type remedies and forward

[47] Initially, RUCO recommends that Qwest make a total contribution to this fund of not less than $6.5 million over five years or more than $14.3 million over seven years. R-1A 25:3-6.

looking remedies. RUCO's hope is that such remedies may reverse some of the damage and provide mechanisms that may prevent similar conduct in the future.[48]

It should be clear at this point that the Commission needs to tighten the regulatory process to insure compliance with the Act and its own Rules. The establishment of a two-part fund would provide the Commission with a mechanism which would allow the Commission to monitor compliance with the Act.[49] A two-part fund would offer CLEC's an easy and efficient way to address their disputes with Qwest before the Commission. With this remedy, the Commission would not only be kept aware of the on-going issues between CLECs and the ILECs, it would allow the Commission to implement the Act. It would also provide the CLECs with a means to address its concerns without fear of reprisal. With a procedure that provides easy access to the Commission, CLECs would not have to consider all the costs and time associated with the more formal process of filing a complaint. R-1A at 26: 16-19. In turn, the Commission would be much more interactive with the CLEC's everyday concerns and could more easily monitor Qwest's conduct. This procedure would discourage Qwest from manipulating its market power and encourage it to cooperate with the Commission.

Another means to assure that Qwest provides acceptable, non-discriminatory service to CLECs would be through rebates or bill credits. The record is replete with instances of service related issues that McLeod and Eschelon had with Qwest. The

---

[48] In making its recommendations, RUCO does not discount Staff's recommendations. Nor does RUCO object to any of Staff's recommendations. In fact, RUCO believes Staff's recommendations are appropriate and can co-exist with RUCO's proposed remedies.

[49] RUCO is recommending that Eschelon and McLeod contribute to this fund initially as a means to redress their involvement in the scheme to defraud the Commission.

service-related disputes with Eschelon were so egregious that Eschelon escalated its dispute to the highest escalation level and ultimately brought the issues directly to the Commission. A rebate or bill credit system would require Qwest to provide a rebate or bill credit to a CLEC in each instance where Qwest provides unacceptably poor service. R-1A at 27: 3-5. This would give Qwest an incentive to provide good service and have the secondary benefit of ameliorating the adverse impact on the CLECs caused by Qwest's poor service quality. R-1A at 27:6-9. Qwest would have the opportunity to report any abuses of this system to the Commission. R-1A at 28: 18-22. This remedy would foster competition by ensuring that CLEC's would not have to pay for inferior service, and providing Qwest with an incentive to provide better service. R-1A at 31:21-32:2.

RUCO's third recommendation is a 10% discount off of the UNE rates Qwest charges. This discount would be made available to all of the CLECs with the exception of McLeod and Eschelon, for no longer than five years. R-1A at 34: 5. Requiring Qwest to make the same terms and conditions available to other CLECs – which would have had the opportunity to opt into these agreements before they were terminated had Qwest complied with the law – is another way the Commission can remedy the competitive imbalance caused by Qwest.

Finally, RUCO recommends that Qwest be required to accelerate its deployment of fiber optic cable and associated broadband-capable electronics. R-1A at 34:18-35:5. The Commission should require Qwest to offer DSL service or its equivalent in all of its central offices by December 31, 2005. Wider availability of DSL benefits consumers in that they would be able to obtain affordable Internet

services at much faster speeds. On the consumer side, the benefits would extend to the rural areas where current unit costs are high and demand for the service is low due to the high costs. R-1A at 39: 2-22. Affordable broadband service may actually enhance the economic viability of these communities. R-1A at 44: 15-17. CLECs would also benefit, provided the Commission requires the fiber optic cables and broadband capable facilities to be made available to the CLECs on an unbundled basis. R-1A at 42:1- 5. By making this recommendation, RUCO is really asking this Commission to require Qwest to carry out on a more expedited basis what it already plans to do. R-1A at 47:22-25.

VIII. CONCLUSION

Qwest knowingly and intentionally violated 47 U.S.C. § 251 and 47 U.S.C. § 252 by not filing interconnection agreements with the Commission. It did so to gain regulatory cooperation from CLECs that might otherwise oppose it and to increase its revenues in an unsteady economic climate. Qwest and McLeod and Qwest and Eschelon carried out schemes to defraud this Commission and the public. The parties' conduct violated A.R.S. § 13-2310 and § 13-2311. In turn, the parties also violated A.R.S. § 40-203. The parties' conduct has stunted the growth of real competition in Arizona, harmed CLECs that are not party to the agreements and tainted several regulatory proceedings.

Based on the foregoing, RUCO respectfully requests that the Commission:

1. Find that Qwest failed to file the terms and conditions contained in the core agreements with the Commission for approval in violation of 47 U.S.C. § 252(e) and A.A.C. R-14-2-1112.

2. Find that, for each of the agreement provisions described in the core agreements, Qwest's conduct in making that provision available to the CLEC party to the agreement was discriminatory to all other CLECs, in violation of 47 U.S.C. § 251.

3. Pursuant to A.R.S. § 40-203, Order Qwest and McLeod and Qwest and Eschelon to cease engaging in schemes to defraud this Commission in violation of A.R.S. § 13-2310 and A.R.S. § 13-2311. RUCO further recommends that the Commission forward the record to the Arizona Attorney General's Office for further consideration.

4. Find that Qwest and McLeod and Qwest and Eschelon entered into illegal and discriminatory agreements in violation of A.R.S. § 40-203.

5. Impose penalties consistent with RUCO's recommendations cited above on Qwest, Eschelon and McLeod.